

§ 1.108-3 Intercompany losses and deductions.

(a) *General rule.* This section applies to certain losses and deductions from the sale, exchange, or other transfer of property between corporations that are members of a consolidated group or a controlled group (an intercompany transaction). See section 267(f) (controlled groups) and § 1.1502-13 (consolidated groups) for applicable definitions. For purposes of determining the attributes to which section 108(b) applies, a loss or deduction not yet taken into account under section 267(f) or § 1.1502-13 (an intercompany loss or deduction) is treated as basis described in section 108(b) that the transferor retains in property. To the extent a loss not yet taken into account is reduced under this section, it cannot subsequently be taken into account under section 267(f) or § 1.1502-13. For example, if S and B are corporations filing a consolidated return, and S sells land with a \$100 basis to B for \$90 and the \$10 loss is deferred under section 267(f) and § 1.1502-13, the deferred loss is treated for purposes of section 108(b) as \$10 of basis that S has in land (even though S has no remaining interest in the land sold to B) and is subject to reduction under section 108(b)(2)(E). Similar principles apply, with appropriate adjustments, if S and B are members of a controlled group and S's loss is deferred only under section 267(f).

(b) *Effective date.* This section applies with respect to discharges of indebtedness occurring on or after September 11, 1995.

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§ 1.108(a)-1 Income from discharge of indebtedness.

(a)(1) Section 108(a) provides a specific exclusion from gross income, at the taxpayer's election, of the amount of income attributable to the discharge of indebtedness, in whole or in part, within the taxable year. In order to take advantage of the exclusion, the taxpayer must file a consent to applicable regulations relating to the adjustment of basis, in accordance with § 1.108(a)-2. This section applies to indebtedness incurred or assumed either (i) by a corporation, or (ii) by an indi-

vidual in connection with property used in his trade or business; and it covers any such indebtedness for which the corporate or individual taxpayer is liable or subject to which the taxpayer holds property.

(2) For purposes of section 108(a) and this section, the determination as to whether an indebtedness is incurred or assumed by an individual in connection with property used in his trade or business depends upon the facts of each particular case. Where an indebtedness (whether secured or unsecured) is incurred or assumed by an individual and where the proceeds of such indebtedness are used to purchase, improve, or repair property used in the trade or business, section 108(a) shall apply to the discharge of such indebtedness. However, an indebtedness of an individual will not be considered as incurred in connection with property used in his trade or business merely because it can be shown that the indebtedness was secured by property used in the trade or business.

(b)(1) If, as of the first day of the taxable year in which a discharge of indebtedness occurs, there is unamortized premium, the amount of the income attributable to such premium shall be excluded from gross income. For example: On January 1, 1955, the M Corporation (which files its return on a calendar year basis) had outstanding an issue of A bonds of the face value of \$10,000, and as of that day there was \$100 unamortized premium on this bond issue. On September 1, 1955, the M Corporation purchased these bonds for \$9,000. The total amount to be excluded from gross income under this section is \$1,100.

(2) If, as of the first day of the taxable year in which a discharge of indebtedness occurs, there is unamortized discount, the amount of the deduction attributable to such discount shall be disallowed as a deduction. For example: On January 1, 1955, the N Corporation (which files its return on a calendar year basis) had outstanding an issue of B bonds of the face value of \$10,000, and as of that day there was \$50 unamortized discount on this bond issue. On September 1, 1955, the N Corporation purchased these bonds for \$9,000. The total amount to be